ORIGINAL

RECEIVED
AUG - 2 1996
FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Federal-State Joint Board	)	**CC Docket No. 96-45**
on Universal Service	)	

DOCKET FILE COPY ORIGINAL

COMMENTS

MCI TELECOMMUNICATIONS CORPORATION

Mary J. Sisak
Donald J. Elardo
1801 Pennsylvania Avenue, N.W.
Washington, D.C. 20554
(202) 887-2605

Chris Frentrup
Senior Regulatory Analyst
1801 Pennsylvania Avenue, N.W.
Washington, D.C. 20006
(202) 887-2731

No. of Copies rec'd 04

Dated: August 2, 1996

SUMMARY

Universal service support must be revised in order to comply with the universal service and the pro-competition provisions of the Telecommunications Act of 1996. Currently, "universal service" is achieved by a combination of mechanisms, some of which are not explicit, which were developed in a monopoly environment and which were based on the incumbent LECs' book costs. These mechanisms simply are no longer appropriate because they would stifle competition by subsidizing the incumbent's inflated costs and inefficiencies. In addition, all support mechanisms which are not explicit are not in compliance with the Act and, therefore, must be eliminated.

Economic models can be used to determine the real amount of universal service support needed in a competitive environment-- an amount equal to the difference between the total service long run incremental cost (TS-LRIC) of providing the local services that should be included in the definition of universal service and the nationwide average rate for local service (approximately $20 per month). Universal service as determined by these models would comply with all of the principles espoused in the Act-- namely, services would be available at just, reasonable and affordable rates; consumers in all regions of the Nation would have access to comparable services at comparable rates; and support would be specific and predictable. A universal service mechanism based on the difference between TS-LRIC and the average rate for local service also would provide the incentive and the funds needed to support infrastructure development and to maintain service quality by allowing LECs to recover the economic cost of providing quality service.

In addition, a TS-LRIC proxy model would promote network efficiency-- one of the major

benefits of competition -- because it is based on forward-looking costs for an efficient network. In this sense, the proxy model is technology-neutral because it does not favor any particular technology. Rather, the model is based on the most efficient technology for the circumstance.

Universal service support based on the nationwide average rate for local service would result in "affordable" service rates for the average consumer. To the extent it is determined that low-income consumers should not pay the nationwide average rate, specific assistance could be targeted to those consumers, like the current Linkup and Lifeline programs.

With respect to eligible schools, libraries and health care providers, the TS-LRIC of providing service should be the starting point for the charge for service to ensure that these entities have access to high quality advanced services at reasonable rates. In addition, further discounts should be given to such entities to account for their size, location and percentage of low-income constituents.

Once the universal service support necessary under this method has been identified, existing support amounts must be removed from LEC rates. In the interstate jurisdiction, this would require the reduction or elimination of the Carrier Common Line (CCL) charge, the current High Cost Fund, Long Term Support, triple-DEM weighting, the Subscriber Line Charge, and the Local Switching charge. The models supported by MCI show that the real amount of support needed to ensure universal service is approximately $4 billion. Accordingly, LEC access charges as identified above must be reduced by at least this amount to prevent double recovery of these costs.

The economic models submitted by MCI can be used to determine universal service support for all companies and in all areas. A different approach should not be necessary for companies in rural areas because the model captures cost differences due to differences in population density. Thus, rural companies with higher costs would have a higher TS-LRIC and, therefore, universal service support would be greater for companies in such areas. The current High Cost Fund should not be retained for companies in rural areas because a different support mechanism for such companies would only encourage sales of exchanges to maximize the subsidy and, thus, increase the amount of support paid by competitors and, ultimately, consumers.

Support payments also should not be based on the LECs' book costs because these costs reflect inefficiencies that might have been acceptable in a monopoly environment, but can no longer be supported if competition is to develop. As an initial matter, a subsidy based on book costs would be far greater than necessary to support universal service. In addition, providing inflated subsidies to incumbent LECs would only make it harder for others to compete against them, both in the local and toll markets.

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Federal-State Joint Board	)	CC Docket No. 96-45
on Universal Service	)	

COMMENTS

MCI Telecommunications Corporation (MCI) hereby submits its response to the request for further comments in the Universal Service Notice of Proposed Rulemaking. MCI's responses to the specific questions asked follow.

Definitions Issues

1. Is it appropriate to assume that current rates for services included within the definition of universal service are affordable, despite variations among companies and service areas?

It is appropriate to assume that current rates for services included within the definition of universal service are affordable, despite variations among companies and service areas, based on the high levels of subscribership, even among low income groups. "Affordability" varies among individuals based on income, personal preference and taste, and individual circumstance. Since it is not possible to determine "affordability" for every individual for the implementation of universal service, the Joint Board and the Commission should evaluate "affordability" based on an "average" consumer. Section 254(b)(1), which establishes the principle that quality services should be available at just, reasonable and affordable rates, does not require that an affordability evaluation be based on differences in income. In fact, the only specific reference to low-income consumers is in Section 254(b)(3), which requires that access to telecommunications and information services be available to low-income consumers "that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas." Thus, a determination of "affordability" based on an average consumer would be in compliance with the Act.

Current subscribership levels indicate that the nationwide average rate would be affordable for the average consumer. If it nevertheless were determined that low-income consumers should not pay the nationwide average rate, specific assistance, such as competitively neutral Linkup and Lifeline programs, should be targeted to those consumers.

2. To what extent should non-rate factors, such as subscribership level, telephone expenditures as a percentage of income, cost of living, or local calling area size be considered in determining the affordability and reasonable comparability of rates?

Universal service support should be based on the difference between the total service long run incremental cost (TS-LRIC) of providing service and the nationwide average rate. This would ensure that all consumers in all areas of the country receive service at "comparable rates".

As indicated in question 1, subscribership levels may be considered an indication of "affordability," however, affordability should be based on an average consumer.

3. When making the "affordability" determination required by Section 254(I) of the Act, what are the advantages and disadvantages of using a specific national benchmark for core services in a proxy model?

Use of a specific national benchmark for core services would simplify administration of the universal service support mechanism, and would ensure that every area could receive service at a reasonable rate. MCI can see no disadvantages.

4. What are the effects on competition if a carrier is denied universal service support because it is technically infeasible for that carrier to provide one or more of the core services?

Any time a carrier is ineligible for support, it would be more difficult for that carrier to compete against the subsidized rate of the company or companies that do receive support. For that reason, the list of core services should be drawn carefully to reflect only those services that are truly necessary. MCI proposes that the services entitled to universal service support should include single party service to the first point of switching, local usage, touch tone, white pages listings, and access to 911, E911, operator services, directory assistance and telecommunications relay service. Most carriers should be capable of providing these services as long as unbundling and resale provisions are adopted which ensure that incumbent local exchange carriers (LECs) make such services available at economically reasonable rates.

5. A number of commenters proposed various services to be included on the list of supported services, including access to directory assistance, emergency assistance, and advanced services. Although the delivery of these services may require a local loop, do loop costs accurately represent the actual cost of providing core services? To the extent that loop costs do not fully represent the costs associated with including a service in the definition of core services, identify and quantify other costs to be considered.

Only access to the core services should receive support, and the local loop provides the access to these services. In addition, there may be some trunking necessary to reach the platforms for some of these services, such as 911 The costs of access, including the loop and trunking, are reflected in both the Benchmark Cost Model (BCM) and the Hatfield studies. The costs for the services themselves, such as directory assistance and advanced services, are recovered in user charges or in some other manner Thus, the loop and truncking costs computed by the models accurately represent the actual cost of providing core services for the purpose of universal service.

Schools, Libraries, Health Care Providers

6. Should the services or functionalities eligible for discounts be specifically limited and identified, or should the discount apply to all available services?

As stated in MCI's recently filed education proposal with the Joint Board, "Connecting Students and Teachers to the Internet: An MCI Proposal," integrating state-of-the-art information technology into schools and libraries and connecting them to the Internet, will provide the opportunity for students to excel. Thus, schools and libraries should have affordable access to every telecommunications service that enhances education. including high speed access to the Internet. MCI has proposed that schools and libraries be charged no more than the economic cost (the TS-LRIC) of any telecommunications service that supports education, and that the Commission encourage high bandwidth connectivity through a set of "Targeted Discounts" that would further reduce the cost of these services. Any definition of high bandwidth services, or advanced services, adopted by the Commission should be flexible enough to include all current services at 1.5 megabits per second and other delivery mechanisms including cable, wireless, and satellite.

7. Does Section 254(h) contemplate that inside wiring or other internal connections to classrooms may be eligible for universal service support of telecommunications services provided to schools and libraries? If so, what is the estimated cost of the inside wiring and other internal connections?

Inside wiring and other internal connections to classrooms are not eligible for universal service support because they are not "telecommunications services" Section 254(c)(1) of the Act states that universal service "is an evolving level of telecommunications services..." . Further, Section 254(h)(1)(A) states that a telecommunications carrier shall...provide telecommunications services which are necessary for the provision of health care services in a State..." ; and Section 254(h)(1)(B) provides that all telecommunications carriers shall provide any of its services that are within the definition of universal service under sub-section (c)(3) to schools and libraries.

"Telecommunications services" are defined as "the offering of telecommunications for a fee directly to the public..."; and "telecommunications" is defined as "the transmission, between or among points specified by the user, of information of the user's choosing, without change in the form or content of the information as sent and received." Inside wiring is not a transmission service and, therefore, it is not a "telecommunications service" eligible for universal service support.

8. To what extent should the provisions of Sections 706 and 708 be considered by the Joint Board and be relied upon to provide advanced services to schools, libraries and health care providers?

Section 706 recognizes the importance of "measures that promote competition in the local telecommunications market" to ensure that the information revolution reaches the nation's schools, libraries, and health care providers. The first step to achieving this goal is vibrant local competition. As such, it is incumbent upon the Joint Board to recommend and the Commission to adopt a universal service mechanism that promotes competition in the marketplace. A competitively neutral Universal Service Fund that supports the economic costs of service will ensure that these goals are all met.

It is equally important, however, as highlighted in Section 706, that the Commission monitor and evaluate progress toward meeting the objectives of improving education through advanced telecommunications services. Therefore, as stated in MCI's education proposal, the Commission should collect and analyze data once a year and publish a comprehensive report on the number of schools and libraries connected, the types of connections and services used, and the number of students served. The data should be set forth by school category (elementary, secondary, other), location (city, suburban, town, rural), region (Northeast, Southeast, Central, West), and enrollment size. The commission should gather similar data for libraries. The Commission should use this data to evaluate the efficacy of its strategy to connect schools and libraries to the Internet, and promote new policies and/or procedures accordingly.

Section 708 is designed to set up a National Education Technology Funding Corporation. This Corporation could be a positive factor in bringing educational technologies to the classroom. Neither the provisions of the new Telecommunications Act -- which cover connectivity to schools and libraries -- nor technology itself, however, are enough to improve educational opportunities. Other elements necessary to introduce educational technologies into classrooms and libraries, including internal networks, hardware and software, teacher training and ongoing support, also must be provided. The Corporation set up under Section 708 could help promote and further the proper introduction of these other elements. However, the Joint Board and the Commission should not rely on the Corporation to address all these enormous tasks. Thus, MCI has proposed the establishment of an Education Technology Council, similar to that proposed by the Aspen Institute.[1] The council would work with state and local officials and other stakeholders to promote strategies for integrating technology into our nation's elementary and secondary schools and libraries.

9. How can universal service support for schools, libraries, and health care providers be structured to promote competition?

Schools, libraries and health care providers should be able to obtain service from the provider of their choice. In addition, the discount provided to these entities should not be in the form of a set price. For example, a school should receive a 10% discount off of TS-LRIC for any company's T-1 connection, rather than be able to obtain a T-1 from any carrier for $200 a month. This would give the school the incentive to find the lowest cost provider since the price to the school would depend

---

[1] The Communications Devolution: Federal, State and Local Relations in Telecommunications Competition, The Aspen Institute, 1995, pp. 35-49.

on the carrier it selects.

10. Should the resale prohibition in Section 254(h)(3) be construed to prohibit only the resale of services to the public for profit, and should it be construed so as to permit end user cost based fees for services? Would construction in this manner facilitate community networks and/or aggregation of purchasing power?

Entities that receive the same level of discount under the universal service mechanism should be allowed to aggregate their purchasing power under sharing arrangements. However, any entity that receives service at a discount under Section 254 should be prohibited from reselling that service in any manner. The Section 254 subsidy is intended to ensure that schools, libraries and health care providers have access to the telecommunications services necessary to serve their constituencies. The subsidy is not intended to be a revenue stream for these entities. Also, allowing resale would lead to levels of support greater than what is necessary to achieve the purposes of the Act and it would deprive competitive telecommunications service providers of customers and revenues, thus impacting their ability to fund universal service.

In addition, Section 254(h)(3) prohibits the "transfer" of network capacity and telecommunications services received by a public institution "in consideration for money or any other thing of value." Thus, it appears that end user fees for services would violate this section.

11. If the answer to the first question in number 10 is "yes," should the discounts be available only for the traffic or network usage attributable to the educational entities that qualify for the Section 254 discounts?

The discounts provided in accordance with Section 254 should be available only for the telecommunications services or network usage attributable to the educational entities that qualify for such discounts.

12. Should discounts be directed to the states in the form of block grants?

13. Should discounts for schools, libraries, and health care providers take the form of direct billing credits for telecommunications services provided to eligible institutions?

14. If the discounts are disbursed as block grants to states or as direct billing credits for schools, libraries, and health care providers, what, if any, measures should be implemented to assure that the funds allocated for discounts are used for their intended purposes?

15. What is the least administratively burdensome requirement that could be used to ensure that requests for supported telecommunications services are bona fide requests within the intent of section 254(h)?

(Response to Questions 12-15)

When determining how to implement discounts for schools, libraries and health care providers, the Joint Board and the Commission should ensure that telecommunications services are available in the most efficient and effective manner, and with the least amount of administrative overhead. In addition, in order for telecommunications service discounts to be effectively used, each community, school and library should develop a comprehensive plan for investing in educational technologies and integrating them into the classroom. While this planning will be up to each local school and library in coordination with parents, community and education leaders, and state and local officials, the Joint Board and the Commission should consider whether to encourage or require schools and libraries to submit a plan to a state agency for approval before receiving a discount under the Act's universal service provisions.

16. What should be the base service prices to which discounts for schools and libraries are applied: (a) total service long-run incremental cost; (b) short-run incremental costs; © best commercially-available rate; (d) tariffed rate; (e) rate established through a competitively-bid contract in which schools and libraries participate; (f) lowest of some group of the above; or (g) some other benchmark? How could the best commercially-available rate be ascertained, in light of the fact that many such rates may be established pursuant to confidential contractual arrangements?

TS-LRIC should be the base service price to which discounts for schools and libraries are applied. This would ensure that eligible services provided to these entities are provided at actual cost and do not include costs for excessive profits or network inefficiencies.

17. How should discounts be applied, if at all, for schools and libraries and rural health care providers that are currently receiving special rates?

To the extent that special rates received by schools and libraries are greater than TS-LRIC minus the discount, they should receive a discount equal to the difference. If the special rates are less than TS-LRIC minus the discount, there should be no additional discount.

18. What states have established discounts programs for telecommunications services provided to schools, libraries, and health care providers? Describe the programs, including the measurable outcomes and the associated costs.

MCI has no information on this.

19. Should an additional discount be given to schools and libraries located in rural, insular, high-cost and economically disadvantaged areas? What percentage of telecommunications services (e.g., Internet services) used by schools and libraries in such areas are or require toll calls?

Discounts should be targeted to low-income, remote and small schools and libraries through tiered discounts provided on a sliding scale. Today, school size, budget and location affect the ability of a particular school to connect to the Internet. According to the U.S. Department of Education, about half of U.S. public schools have access to the Internet. Yet only 31% of schools with a large proportion of students from low-income families have access to the Internet, as compared to 62% of schools with relatively few students from low-income families. In addition, only 39% of schools with fewer than 300 students are connected to the Internet, as compared to 69% of schools with more than 1,000 students.[2]

---

[2] Advanced Telecommunications in U.S. Public Elementary and Secondary Schools, United States Department of Education, National Center for Education Statistics, 1995.

<u>20. Should the Commission use some existing model to determine the degree to which a school is disadvantaged (e.g., Title I or the national school lunch program)? Which one? What, if any, modifications should the Commission make to that model?</u>

The national school lunch program may be an accurate measure in determining a discount scale.

<u>21. Should the Commission use a sliding scale approach (i.e., along a continuum of need) or a step approach (e.g., the Lifeline assistance program or the national school lunch program) to allocate any additional consideration given to schools and libraries located in rural, insular, high-cost, and economically disadvantaged areas?</u>

There are many ways to structure tiered discounts such as a sliding scale based on the economic status of a school's students or library's users For example, discounts could be provided on a sliding scale in proportion to the percentage of students from low-income families as defined by the Department of Education. Discounts also could be structured to enable smaller schools and schools in high cost areas to purchase advanced telecommunications as well.

<u>22. Should separate funding mechanisms be established for schools and libraries and for rural health care providers?</u>

If the Commission adopts an interstate-only universal service fund, then there must be separate funding mechanisms for schools and libraries and rural health care providers because all telecommunications service providers must contribute to the latter and only interstate carriers would contribute to the former.

<u>23. Are the cost estimates contained in the McKinsey Report and NII KickStart Initiative an accurate funding estimate for the discount provisions for schools and libraries, assuming that tariffed rates are used as the base prices?</u>

The cost estimates in these documents appear to accurately reflect tariffed rates.

24. Are there other cost estimates available that can serve as the basis for establishing a funding estimate for the discount provisions applicable to schools and libraries and to rural health care providers?

TS-LRIC should be adopted as the basis for establishing the funding estimate for the discount provisions.

25. Are there any specific cost estimates that address the discount funding estimates for eligible private schools?

There is no reason to believe that the per-school cost estimates for private schools would be different than the cost estimates for public schools. Thus, the existing per-school cost estimates for public schools can be used for private schools as well

High Cost Fund

General Questions

26. If the existing high-cost support mechanism remains in place (on either a permanent or temporary basis), what modifications, if any, are required to comply with the Telecommunications Act of 1996?

The existing high-cost mechanism should not remain in place. Support should be based on the difference between the nation-wide average rate and the economic cost of providing local service. Setting support based on this level would ensure that all areas of the country have comparable rates, and would allow the companies paying for the universal service mechanism to avoid having to fund the inefficiencies of the incumbent LECs. In conjunction with this new universal service mechanism, implicit support recovered in access charges must be eliminated

The implicit support reflected in the Carrier Common Line (CCL) charge and the Interconnection Charge (IC) are no longer allowed under the 1996 Act, and must be reduced or eliminated and replaced with explicit funding. The triple-dial equipment minute (DEM) weighting, which allows up to three times more of the switching costs to be assigned to the interstate jurisdiction, based on the number of lines served by the company, also must be eliminated and replaced with explicit funding.[3] As it currently exists, triple-DEM weighting is neither explicit nor recovered from all telecommunications carriers.

27. If the high-cost support system is kept in place for rural areas, how should it be modified to target the fund better and consistently with the Telecommunications Act of 1996?

The Commission should not adopt different support mechanisms for different classes of companies. Doing so will only encourage sales of exchanges to the company which will receive the maximum subsidy. If the Commission nevertheless decides to treat rural carriers differently, the modifications discussed in the answer to question 26 supra would be necessary.

28. What are the potential advantages and disadvantages of basing the payments to competitive carriers on the book costs of the incumbent local exchange carrier operating in the same service area?

The only advantage is that it would be administratively simple. However, since the incumbent LECs' book costs are likely to include many inefficiencies and thus be higher than necessary, it would result in the competitive LECs receiving more support than they need. While the competitive carriers would presumably pass this support to end users, the fund would be larger than necessary to ensure universal service. Basing support on TS-LRIC would ensure that LEC inefficiencies are not funded.

---

[3] Even if this triple DEM weighting is retained, it must be revised. Under the current rules, increased assignment to the interstate jurisdiction occurs when a company has 50,000 or fewer lines. However, data filed by the small carriers themselves shows that increased cost, if any, occurs only if a company has 1,000 or fewer lines. See, e.g., OPASTCO Comments, filed October 10, 1995 in CC Docket No. 80-286, at Appendix B, Figure 4A and 4B.

29. Should price cap companies be eligible for high-cost support, and if not, how would the exclusion of price cap carriers be consistent with the provisions of section 214(e) of the Communications Act? In the alternative, should high-cost support be structured differently for price carriers than for other carriers?

Price cap companies should be eligible for high-cost support computed as advocated in answer to question 26, supra. Price cap companies should not, however, be eligible for high-cost support that is computed based on their book costs Providing support to price cap carriers based on their book costs would weaken the incentives for cost-cutting that price caps is intended to provide.

Support should not be structured differently for price cap and non-price cap companies, as that would merely encourage sales of exchanges to the company that would receive the maximum support. It also would reinforce the incentives that rate of return regulated carriers have to be inefficient and to cross-subsidize.

30. If price cap companies are not eligible for support or receive high-cost support on a different basis than other carriers, what should be the definition of a "price cap" company? Would companies participating in a state, but not a federal, price cap plan be deemed price cap companies? Should there be a distinction between carriers operating under price caps and carriers that have agreed, for a specified period of time, to limit increases in some or all rates as part of a "social contract" regulatory approach?

The only justification for treating price cap carriers differently is to avoid weakening the incentives price cap regulation provides. As long as the computation of universal service support is divorced from the LEC's booked costs, providing support to a price cap LEC would not weaken the price caps incentives it faces If, however, support is based on a LEC's booked costs, then providing that support would dilute the price cap incentives, and the company should be ineligible for universal service support.

The definition of "price cap company" in this case would depend on whether the Commission adopts a unitary fund or an interstate-only fund. If the Commission adopts an interstate-only fund, price cap companies should be those companies under price cap regulation at the federal level. If the Commission adopts a unitary fund, price cap companies should be companies that are under price cap regulation in either jurisdiction. This would avoid diluting the incentives that a company faces under price caps. Because both an explicit price cap plan and a "social contract" at least partially break the link between rates and costs, LECs under either of these types of regulation should be ineligible for support if that support is computed based on the LEC's own costs.

31. If a bifurcated plan that would allow the use of book costs (instead of proxy costs) were used for rural companies, how should rural companies be defined?

A bifurcated plan should not be adopted, as that would encourage the sale of exchanges to receive the maximum subsidy. It also would continue a method for universal service funding that the Commission and Joint Board have already determined results in excessive support levels, as evidenced by their decisions to cap the existing fund and to review the previous fund. The cost models on the record all include the effect of lower population density on costs; thus, the models should accurately reflect the nature of costs in the more rural areas.

If the Commission nevertheless adopts a bifurcated approach, the companies that receive support based on their book costs should be very limited. For example, data placed on the record by the rural companies in this docket show that switching costs per line do not increase until a company serves fewer than 1,000 lines, rather than the 50,000 lines at which the current triple-DEM weighting rules apply.[4] Thus, rural companies should be limited to those serving fewer than 1,000 lines.[5]

---

[4] Ibid.

[5] See answer 26 supra.

<u>32. If such a bifurcated approach is used, should those carriers initially allowed to use book costs eventually transition to a proxy system or a system of competitive bidding? If these companies are transitioned from book costs, how long should the transition be? What would be the basis for high-cost assistance to competitors under a bifurcated approach, both initially and during a transition period?</u>

Any transition adopted should be very short, to minimize the incentive and ability to trade exchanges to maximize the subsidy. Three years would be sufficiently long to allow the companies to adjust to the new level of support, while being short enough to make it unlikely that a sale of exchange could be identified, consummated, and pay off in a higher subsidy payment.

During a transition period, support should be based on a weighted average of the support computed under the two methods. In the first year, the support would be based one fourth on the new system and three fourths on the old system. In the second year, support would be based half on the new system and half on the old system. In the final transition year, support would be based three fourths on the new system and one fourth on the old system. In the fourth and subsequent years, support would be based only on the new system

New entrants should be entitled to the same level of support as the incumbents during the transition. This would ensure that neither company has a competitive advantage based on the support mechanism, and would minimize the regulatory burden on the new entrant. Because the transition period is so short, there would be less risk of the fund being too large and because of competitive pressure there would be very little risk of the new entrant receiving excessive support, as discussed in the answer to question 28, <u>supra</u>.

33. If a proxy model is used, should carriers serving areas with subscription below a certain level continue to receive assistance at levels currently produced under the HCF and DEM weighting subsidies?

Computation of support based on a proxy model would provide all the support a company would need to be able to provide service at an acceptable rate. It would also allow the removal of implicit support from access charges. There should be no need for additional support beyond that level. In any event, differences in subscribership levels, which have persisted in spite of the existing high cost fund (HCF) and DEM weighting, indicate that these mechanisms are not the answer. Thus, additional support based on the existing HCF and DEM weighting mechanisms would not be a solution to the problem.

In addition, as a practical matter, if the Commission continues these support mechanisms for areas with low penetration rates, a much larger data collection than that which is currently employed would be required. At present, the Commission's monitoring of penetration levels is based on a survey performed under contract by the Census. This survey provides estimates of penetration levels for each state. To obtain estimates of penetration levels for each company's service area, the sample of households would have to be greatly increased, with a concomitant increase in cost. Alternatively, the Commission could obtain data on subscribership from the LECs , but would then have to know the count of households in each area, and would have to be sure it had subscriber counts from all LECs serving an area. In either case, the cost of computing the penetration levels would be substantially higher than it is today.

Proxy Models

34. What, if any, programs (in addition to those aimed at high-cost areas) are needed to ensure that insular areas have affordable telecommunications service?

There is no evidence that additional programs are needed to ensure that insular areas have affordable local telecommunications service. In addition, the Commission is examining pricing of interexchange service in certain insular areas in CC Docket No. 96-61, Phase I. No additional examination of this question is needed in this docket.

35. US West has stated that an industry task force "could develop a final model process utilizing consensus model assumptions and input data," US West comments at 10. Comment on US West's statement, discussing potential legal issues and practical considerations in light of the requirement under the 1996 Act that the Commission take final action in this proceeding within six months of the Joint Board's recommended decision.

It is highly unlikely that such consensus could be reached or that it could be reached so that the Commission could take final action in this proceeding within six months of the Joint Board's recommended decision. Because of the number of interested parties to such a process -- LECs, interexchange carriers (IXCs), other telecommunications companies that would be liable for funding universal service support, and user groups, to name a few -- it would be difficult to constitute a task force in the time frame available to the Commission and Joint Board, let alone have that task force achieve consensus.

Also, the parties would have widely diverging interests and, therefore, achieving consensus would be very difficult. This difficulty is evident in the original BCM filing, in which the Joint Sponsors, failing to agree on the cost factors to be used, presented two sets of results. This difficulty is made even more evident by the latest filing of BCM results.[6] Two of the original four sponsors

[6] See, Letter from Jay Keithley and Glenn Brown to William F. Caton, filed July 3, 1996, CC Docket No. 96-45.

were not involved in submitting the latest version of BCM. MCI does not know why NYNEX was not involved, but in MCI's case this was due to the other parties simply ceasing to solicit our input on modifications to the BCM. At some point, U S West and Sprint decided to further develop the BCM on their own, and did not inform MCI of that decision [7] In fact, MCI became aware that the BCM had been revised only when the filing was made by U S West and Sprint.

Finally, an "industry task force" could achieve consensus only if there is a good faith willingness on the part of all parties to reach consensus. Because incumbent LECs have the most to lose when competition in the local market emerges and the most knowledge about many costing issues, they would have little incentive to engage in the kind of negotiation required to reach consensus.

36. What proposals, if any, have been considered by interested parties to harmonize the differences among the various proxy cost proposals? What results have been achieved?

The various models placed on the record in this proceeding agree in general approach, i.e., determine the forward-looking costs of building a network today that will provide the services that make up universal service. Where they differ is in how to estimate those costs. For instance, the costs estimated in the first version of BCM using the forward-looking cost factor were slightly lower than the costs estimated by the original Hatfield model. However, the second version of BCM has revised several assumptions used to estimate the cost, and now the costs estimated by that model greatly exceed the costs estimated by Hatfield. Consistent assumptions about network design and

[7] MCI's last meeting with U S West and Sprint was on April 16, at which the companies agreed to make modifications to the BCM, and to reconvene at a later date to review the results of those modifications. MCI was never notified of the meeting at which those results were reviewed. In fact, in a conversation in June with one of the co-sponsors, MCI was told that new model results had not been developed.

cost factors should result in consistent model results.

37. How does a proxy model determine costs for providing only the defined universal service core services?

The first step in building a proxy cost model is to define the universal service core services. The network is then designed to deliver those core services. The proxy cost model then determines the investment necessary to build a network of that design, and the cost of the network is determined by the application of cost factors to that investment

38. How should a proxy model evolve to account for changes in the definition of core services or in the technical capabilities of various types of facilities?

When core services are re-defined, the network that the proxy model embodies must be evaluated to determine whether it needs to be re-designed to reflect the new core service(s). If it does, then the proxy cost model must be modified to reflect the new network design. Because the cost proxy model reflects the best current technology and because the services to be included in the definition of universal service are likely to evolve slowly, the necessary modifications can likely be performed incrementally, with new features added to the existing network, rather than the entire network being re-engineered

39. Should a proxy model account for the cost of access to advanced telecommunications and information services, as referenced in section 254(b) of the Act? If so, how should this occur?

The proxy model should account for the costs of providing all services included in the Commission's definition under Section 254© of the services which are eligible for universal service support. To the extent the Commission determines that access to the advanced services referred to in Section 254(b) should be eligible for support, the proxy cost model must reflect the cost of that access.

MCI believes that basic universal service should include single party service to the first point of switching, local usage, touch tone, white pages listings, access to 911, E911, operator services, directory assistance, and telecommunications relay service. The Hatfield and BCM cost models filed in this docket reflect these services.

<u>40. If a proxy model is used, what, if any, measures are necessary to assure that urban rates and rates in rural, insular, and high-cost areas are reasonably comparable, as required in Section 254(b)(3) of the 1996 Act?</u>

If support is set as MCI advocates at the difference between the nation-wide average rate and the TS-LRIC of the service, then rates in urban, rural, insular, and high-cost areas could be set at comparable levels, namely, the nation-wide average rate, because charges for local rates set by the State commissions would reflect the support the local exchange companies receive.

Some parties have suggested that rates would not be reasonably comparable because some local calling areas are larger or contain more telephone subscribers than others. In other words, although the rates may be comparable, the value of the service is not. The Joint Board and the Commission should leave any such determinations concerning the appropriateness of designated local calling areas to the state commissions.

<u>41. How should support be calculated for those areas (e.g., insular areas and Alaska) that are not included under the proxy model?</u>

There is no reason why all areas cannot be modeled. Once the Commission and Joint Board have adopted a model, those companies that wish to receive universal service support should be required to provide the data necessary to run the model. If certain data is not available, the companies should suggest alternative sources of data that would allow the model to be run.[8]

---

[8] For instance, the original BCM had no estimate for the costs of service in Alaska because there was no terrain data available for that state. Since the terrain data was used only to

42. Will support calculated using a proxy model provide sufficient incentive to support infrastructure development and maintain quality service?

A proxy cost model that computes the TS-LRIC of a service would allow the LEC to recover the economic cost of providing quality service. Since the full economic cost of the service would be recovered either from end users or from the universal service fund, the LEC would have the incentive and the funds to support infrastructure development and maintain service quality.

43. Should there be recourse for companies whose book costs are substantially above the costs projected for them under a proxy model? If so, under what conditions (for example, at what cost levels above the proxy amount) should carriers be granted a waiver allowing alternative treatment? What standards should be used when considering such requests?

Carriers should not be granted special treatment solely because their book costs differ substantially from the costs derived from a proxy model. In those few areas where a carrier becomes unwilling and unable to serve an area at the price and universal service support level determined by the proxy model, the area should be put out to bid by any company to provide service.[9] Companies would bid their required support payment to serve an area, with the lowest bidder determining the support level for that area. Any carrier willing to provide service in that area would then be eligible to receive support at the level submitted by the lowest bidder. If the incumbent LEC was not the winning bidder, it would have to make its network available for resale at net book value to the

---

determine whether the placement costs were high, a company in such an area could provide to the Commission verifiable information on the terrain, without having to use the detailed terrain data provided by the United States Geological Service, as was done for the other states for which the data were available.

[9] Before it can be eligible for this process, the LEC must face a heavy burden of proof. It should not be sufficient for the LEC to claim that its book costs exceed model costs, or equivalently, that its earnings are very low. The LEC must be able to show why it is impossible for it to provide service at the cost estimated by the model, or must be seeking permission from the State commission to withdraw from providing service to that area.